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IN THE

Supreme Court of the United States

OCTOBER TERM, 1952

NO. 79.

MARTHA L. ALISON

v.

THE UNITED STATES OF AMERICA.

On Certificate From the United States Court of Appeals for the Third Circuit.

BRIEF FOR MARTHA L. ALISON, Plaintiff-Appellant.

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OPINIONS BELOW.

The Opinion of the District Court (R. 5, 6, 7 and 8) is reported at 97 F. Supp., 959.

The Court of Appeals did not file an Opinion, but certified a question of law involved to this Court (R. 11) concerning which it desired instruction for the proper decision of the case. This Court ordered the entire record sent up so that it may decide the entire matter in controversy (R. 11).

JURISDICTION.

This Court has jurisdiction by virtue of 28 U.S.C., Section 1254 (3). The judgment to be reviewed was entered by the District Court for the Western District of Pennsylvania on May 17, 1951 (R. 10).

QUESTION PRESENTED.

Where a taxpayer sustains a loss by embezzlement, the fact of embezzlement and the exact dates of each separate act of embezzlement being unknown to her, is the embezzlement or theft loss deductible from gross income by the taxpayer for the taxable year in which the embezzlement or theft loss is discovered, under Section 23 (e) of the *Internal Revenue Code,* 26 U.S.C.A. 23 (e)?

STATUTES AND REGULATIONS INVOLVED.

Internal Revenue Code:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * * * *

(e) LOSSES BY INDIVIDUALS.—In the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

* * * * * * *

(3) of property not connected with the trade or business, if the loss arises from fires, storms, shipwreck, or other casualty, or from theft. * * *

* * * * * * *

(26 U. S. C. 1946 ed., Sec. 23.)

SEC. 43. PERIOD FOR WHICH DEDUCTIONS AND CREDITS TAKEN.

The deductions and credits * * * provided for in this chapter shall be taken for the taxable year in which "paid or accrued" or "paid or incurred", dependent upon the method of accounting upon the basis of which the net income is computed, unless in order to clearly reflect the income the deductions or credits should be taken as of a different period. * * *

(26 U. S. C. 1946 ed., Sec. 43.)

Treasury Regulations 103, promulgated under the Internal Revenue Code:

SEC. 19.23 (e)-1. *Losses by Individuals.*— Losses sustained by individual citizens or residents of the United States and not compensated for by insurance or otherwise are fully deductible if * * * (c) arising from fires, storms, shipwreck, or other casualty, or theft, * * *.

SEC. 19.43-2. *When Charges Deductible.*— * * * A loss from theft or embezzlement occurring in one year and discovered in another is ordinarily deductible for the year in which sustained.

STATEMENT.

In this case, Martha L. Alison, appellant in the Court below, and who will hereinafter be referred to as the taxpayer or appellant, seeks to recover from the United States of America, the sum of $2843.78, plus interest, as the result of an overpayment of her income tax for the year 1941. The case in the District Court was tried by the Court without a jury, upon the pleadings and the written Stipulation of the facts.

The action was brought against the United States of America pursuant to the provisions of Section 24 of the *Judicial Code,* as amended, 28 U.S.C.A., Section 41 (20).

The action arises under the Internal Revenue Laws of the United States and the applicable statute is Section 23 (e) of the *Internal Revenue Code,* 26 U.S.C.A. Section 23 (3), which provides as follows:

> "In computing net income there shall be allowed as deductions * * * (e) in the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise * * * (3) or from theft."

Appellant taxpayer in this case filed her income tax return for the year 1941, but inadvertently failed to deduct from her gross income a loss sustained by her on November 24, 1941 in the amount of $21,804.90, which resulted in an overpayment of her income tax in the amount of $2,843.78. She thereafter, on or about March 30, 1943, filed a claim for refund for the year 1941 for this overpayment, which claim for refund was disallowed by the Commissioner of Internal Revenue on the theory that the loss which was claimed as a deduction for the

year 1941 was an embezzlement attributable to the years 1931 to 1940, and did not occur in 1941.

Suit was filed in the Court below for the refund pursuant to the provisions of Section 24 of the *Judicial Code* as amended, 28 U.S.C.A., Section 41 (20), on the theory that the fact of embezzlement was not known and the loss was not discovered or sustained until the year 1941, and that deduction for this loss should have been allowed for the year 1941 under the statutes and decisions arising thereunder.

One J. W. Cree, prior to his death on November 24, 1941, was the manager of several trust estates and also a business agent and adviser for a large number of persons. Among his clients was the appellant in this case, whose maiden name was Martha Liggett. When the appellant was a minor, Mr. Cree was her guardian, and after she became of age, Mr. Cree continued as her business agent and adviser. The appellant's chief source of income was from real estate and securities and Mr. Cree had complete control and possession of the funds and property of the appellant. There was no written agreement between the appellant and Mr. Cree respecting the funds and securities and no accounting was ever requested or given by Mr. Cree. The account of the appellant, as well as other trust accounts, was carried in a separate set of books called the "J. W. Cree, Jr., Trust Account", the funds of which were commingled with his own personal funds. The securities were likewise carried in the name of J. W. Cree, Jr. None of these latter facts were known to appellant until after the death of said Cree (R. 9).

Shortly after the death of Mr. Cree, the appellant found from an examination of his books and records

that there was due her cash in the amount of $30,155.37, which sum was not available for the reason that Mr. Cree had commingled those funds with those of his own and had been using them for his personal benefit. The appellant was the largest creditor of Mr. Cree's estate and inasmuch as the estate did not have sufficient funds to pay all creditors, an agreement was reached whereby the appellant took a loss of $21,804.90 on her claim, which included a cash payment of $3,380.95 to the appellant by a creditor of Mr. Cree's estate. This cash payment was made to the appellant under date of November 18, 1942. After these transactions were completed the appellant's loss arising out of the settlement amounted to $21,804.90 (R. 9).

Throughout the period from 1931 to the date of Mr. Cree's death on November 24, 1941, Mr. Cree was a director in several banks and prominent in real estate circles as well as in business circles in the City of Pittsburgh. He enjoyed substantial credit and had a reputation of meeting all his obligations as they accrued (R. 10).

The amounts taken by Mr. Cree and the amounts paid back to the appellant, as shown by Mr. Cree's personal books, which were discovered for the first time after his death and of which appellant had no knowledge, are as follows (R. 4):

Years	Amount Taken	Amount Paid Back	Net Amount Embezzled
1931	$ 8,000.00	$2,000.00	$ 6,000.00
1932	500.00	.....	500.00
1934	2,000.00	.....	2,000.00
1935	3,000.00	.....	3,000.00
1936	4,800.00	500.00	4,300.00
1937	2,000.00	.....	2,000.00
1938	4,950.00	1,450.00	3,500.00
1939	4,300.00	.....	4,300.00
1940	1,500.00	.....	1,500.00
1941	.....	.....	.....
	$31,050.00	$3,950.00	$27,100.00
Add: "Uninvested principal in principal (stock) Acc't"			3,055.37
Total uninvested cash embezzled			$30,155.37

The appellant had no reason to suspect that any of her funds were being embezzled by Mr. Cree and had no knowledge of such embezzlement until after his death (R. 4).

Taxpayer's chief source of income was from real estate and securities, and Mr. Cree had complete control and possession of the funds and property of the appellant, and it is also stated that there was no accounting nor was one ever requested, or given by Mr. Cree (R. 3). This is not to be construed to mean that Mr. Cree during the period from 1926, when Mr. Cree ceased to be appellant's legal guardian, until the time of his death on November 24, 1941, failed to account for income received on appellant's property and investments. Accounting for income and payment thereof to the appel-

lant was made regularly up to the time of Mr. Cree's death.

The District Court was of the opinion that the plaintiff was entitled to take the deduction in the year of discovery (R. 7) but felt bound by precedent in this Circuit (*First National Bank of Sharon, Pa. v. Heiner*, 66 Fed. 2d. 925 (1933) to hold against her. Had it not been for this decision, the Court would have followed the later decision of the First Circuit in *Boston Consolidated Gas Co. v. Commissioner of Internal Revenue*, 128 Fed. 2d. 473 (1942) and found in her favor (R. 7).

On appeal by the taxpayer to the Court of Appeals, after two oral arguments, that Court was unable to arrive at a decision and, after certification of the question of law involved, the entire record is now before this Honorable Court for final disposition.

SUMMARY OF ARGUMENT.

It is the contention of appellant that under all of the facts of this case, the law applicable thereto and the decisions of this and lower Courts, that she is entitled to deduct the loss by embezzlement for the year 1941 when it was discovered by her, and that the decision of the District Court was erroneous. The taxpayer did not sustain a deductible loss until, upon the death of the embezzler in 1941, the defalcation was discovered. That is the identifiable event which fixes the time for the deduction.

As held by this Court in *Commissioner v. Wilcox*, 327 U.S., 404 (1946) an embezzler, when appropriating money, incurs a continuous obligation to repay, and the

embezzled money does not constitute taxable income to him.

It is admitted that the taxpayer in this case had absolutely no knowledge of the misappropriation of her property, and the secret records of the Trustee were discovered only after his death. They may or may not have represented the actual facts, but apparently it was a record of the amount he owed to his principal, which only came to light by reason of his death.

In the Court below, counsel for the Government argued that it was the gist of taxpayer's contention that the taxable period within which a deduction for a loss arising from embezzlement must be taken is to be determined solely by a subjective test and that this contention was specifically rejected by this Court in *Boehm v. Commissioner*, 326 U.S., 287 (1945).

Counsel here contends that the question of a subjective test is not involved in this case and, on the contrary, the fact of the discovery of the embezzlement and the death of the embezzler are objective events which have nothing whatever to do with the state of the taxpayer's mind.

The *Boehm Case* cited by the Government in support of its contention is not in point because, in that case, the issue was when certain corporate stock became worthless for income tax purposes. The taxpayer contended that he could determine this time solely on his opinion as to when the stock became worthless.

The Court held, however, that this was a question of fact for The Tax Court to determine since the facts showed a succession of identifiable events which occurred prior to the year contended so as to justify the

conclusion that the stock was worthless prior to the year claimed by the taxpayer.

The facts in this case are that the state of the taxpayer's mind is not involved since it was stipulated that the bona fide discovery of the embezzlement was made in 1941 and that taxpayer had no knowledge of or reason to know of the embezzlement prior to the death of the Trustee (R. 10).

The Government further contended in its argument below that the decision of the Court of Appeals in the case of *Boston Consolidated Gas Co. v. Commissioner*, 128 Fed. 2d, 473, is a clear departure from the plain intent of the statute and from the principles enunciated by the Supreme Court, and should be overruled.

It is our contention that the said *Boston Consolidated Gas Co. Case* is in full accord with the law. It has since been followed by decisions in The Tax Court and acquiesced in by the Commissioner of Internal Revenue, and should be decisive of the issue involved in this case.

The Government contends that the *Boston Consolidated Gas Co. Case* is in effect a judicial amendment of statutes. With this we do not agree, and contend that the decision is an interpretation of the statute and the regulations which should be followed.

The cases are in confusion as to the period in which embezzlement losses are deductible. In the first place, Congress created uncertainty when it stated that losses by individuals are deductible in the year in which "sustained", without defining what was meant by "sustained". The word has different meanings, and in such losses as those by embezzlement, which are unknown losses and which, by their very nature, stand in a category of their

own, it is clear that a loss is not sustained until discovered, regardless of when it actually occurred.

The Treasury Department's Regulation (P. 10) sustains the taxpayer's position by providing that embezzlement losses are *ordinarily* deductible for the year in which sustained. From this language it would seem that the Government itself contemplates certain situations wherein the deduction would be allowable in a year other than the year in which the loss occurs.

In view of the above, it is obvious that the Court of Appeals in the First Circuit, in the *Boston Consolidated Gas Co. Case, supra,* clarified by judicial action a law where uncertainty existed. This is fully justified under the wording of the statute and the regulation because the Treasury Department, in using the word "ordinarily", contemplates that certain situations might give rise to different treatment, and since the statute and the regulation fail to specify the situation, it is certainly within the power of the Court to do so.

The running of the statutory time limit for claiming a refund should be considered a special case calling for allowance of the deduction in the year of *bona fide* discovery so far as embezzlement losses are concerned.

ARGUMENT.

I.

The Loss Did Not Occur Until 1941.

According to the record in this case, Mr. Cree, the embezzler, had acted as guardian for the appellant until she became of age and thereafter until the time of his death on November 24, 1941, acted as agent and trustee for the appellant, and it must be assumed that since there is nothing to indicate otherwise, Mr. Cree discharged his duties as guardian in a manner beyond reproach. He was also manager of several trust estates, was a director in several banks and prominent in real estate circles, as well as in business circles in the City of Pittsburgh, enjoyed a substantial credit and had a reputation of meeting all his obligations as they accrued. For this reason, as well as her implicit confidence in Mr. Cree, the appellant did not have the slightest suspicion of what was discovered upon his death. There is nothing whatever in the relationship between these parties, and keeping in mind the reputation of Mr. Cree, that appellant would have any way whatsoever of ascertaining that any of her property had been misappropriated until the time of Mr. Cree's death.

According to the Stipulation, Mr. Cree's books, as set forth in the Statement of the Case, indicated that certain amounts of money were taken at various times beginning in 1931 and ending in 1940. Appellant was in complete ignorance of these facts and even though Mr. Cree's personal books may have indicated to the Commissioner of Internal Revenue that the embezzlement took place in the years indicated, we do not agree

with his conclusion. It is quite clear from the facts of the case that had the appellant at any time during Cree's life time, made claim for any money due her from him, he would, by reason of his financial connections, excellent credit and reputation, have been able to and would actually have made payment to appellant of the full amount due and owing by him to her. His death and the condition of his estate made repayment to appellant of the full sum due her impossible. The result was that the moneys taken and used by Cree and which he could have paid at any time up to his death in 1941 were, because of Cree's fiduciary relation to plaintiff, as a matter of fact embezzled, but could not be considered as such until it was discovered and ascertained in the year 1941.

We refer the Court to the concurring Opinion of Magruder, Circuit Judge, in *Boston Consolidated Gas Company v. Commissioner of Internal Revenue*, 128 Fed. 2nd, 473 (First Circuit, 1942), in which he considers that analytically the taxpayer did not sustain a loss at the time of the embezzlement from its cash account. The money in the embezzler's hands still belonged to the taxpayer, and at most there had only been a change in the form of the taxpayer's assets. He further held, page 477:

> "In the recent case of McKnight v. Commissioner, 127 F. 2d 572, decided by the Circuit Court of Appeals for the Fifth Circuit, April 29, 1942, it was held that the embezzler of money, who is unable to restore it, does not make a taxable gain thereby. The court said: 'By the taking the embezzler incurs an equivalent debt as surely as if he had borrowed with the consent of the owner. The first takings are, indeed, nearly always with the intention of re-

paying, a sort of unauthorized borrowing. It must be conceded that no gain is realized by borrowing, because of the offsetting obligation. This would be true even though at the time there was no intention to repay. It seems to us that the same thing is true of each act of embezzlement.' If at the time of the embezzlement the wrongdoer makes no gain, because of the offsetting obligation, it seem logical to hold that the person whose money is taken does not at that time sustain a loss. Cf. Douglas County Light & Water Co. v. Commissioner, 9 Cir., 1930, 43 F. 2d 904. Logic here coincides with practical convenience, because, as pointed out by Judge Woodbury, if the Government's view is accepted, the wronged party will often be deprived unjustly of a tax deduction through inability to prove the specific amounts embezzled in any particular year. The same injustice would also result if the taxpayer did not discover an embezzlement until too late to file an amended return and to claim a refund for the year in which the money was taken."

II.

Statutes Authorizing Deductions Should Be Liberally Construed.

The Courts have held that provisions of the statute authorizing a taxpayer to deduct losses in computing income tax, being relief measures, should be liberally construed in favor of the taxpayer. *Burnet, Commissioner of Internal Revenue, v. Marston,* 57 Fed. 2d, 611. Also, it has been held that Internal Revenue Laws should be construed and applied with a view of avoiding, so far as possible, unjust and oppressive consequences. *Farmers Loan and Trust Co. v. Minnesota,* 280 U.S., 204, 212. *Lucas v. American Coat Co.,* 280 U.S. 445, in which it is said:

> "The general requirement that losses be deducted in the year in which they are sustained calls for a practical, not a legal, test."

As will be noted by referring to the Statement of the Case, if the appellant in this case is not permitted to deduct her loss for the year 1941, she is forever precluded from asserting the deduction for any other years for the reason that she did not discover the embezzlement until too late to file an amended return and to claim a refund for the year in which the money was taken. According to the books, the money was taken during the years 1931 to 1940, inclusive, and by the time the Commissioner of Internal Revenue had acted on the claim for refund in the 1942 return, it was too late for the appellant to file claims for refund for the years in question. This certainly works an unjust and oppressive consequence which is not sanctioned by the Courts.

In the case of taxes imposed by the 1934 or subsequent Acts, the period of limitation is three years from the time the return was filed, or two years from the time the tax was paid, whichever expires later (Int. Rev. Code, Sec. 322). In case of taxes imposed by the 1932 and 1928 Acts, the limitation is two years from the time the tax was paid.

Keeping the above limitation in mind, the taxpayer would be deprived entirely of any right to charge off the embezzlements alleged to have occurred during the years 193[illegible] to 1937, inclusive, in the total amount of $17,800.00, which was disclosed solely by Mr. Cree's personal books, and of which the taxpayer had no knowledge.

To be practical and to promote uniformity, the year of bona fide discovery should be the criterion.

III.

Embezzlement Losses Should Be Deductible in the Year of Discovery.

It is respectfully contended that the decision of the First Circuit Court of Appeals in the case of *Boston Consolidated Gas Company v. Commissioner of Internal Revenue,* 128 Fed. 2d, 473, decided in 1942, and since followed by decisions in other Courts, should be approved by this Honorable Court, and the law set forth therein clearly established as the law of the land.

In that case the petitioner's treasurer and head cashier died on January 30, 1935, having last worked on January 21st of that year. An audit of the petitioner's books made during 1935 showed that he had embezzled $99,139.09, $98,323.55 of which had been embezzled before December 31, 1934. No shortage through embez-

zlement was brought to light by an audit of the petitioner's books in 1933 and 1934 and in 1935 taxpayer claimed as a deduction in its 1935 income tax return the shortage ascertained to be $61,539.94. The Commissioner and the Board of Tax Appeals refused to allow the deduction on the ground that the loss must be deducted in the year in which it is sustained even though it is not discovered until a later year. The Circuit Court, in reversing the Board of Tax Appeals (Woodbury, Circuit Judge), held:

> "So far as we can determine the Supreme Court of the United States has not spoken on this question except to say by way of dictum in Burnet v. Huff, 288 U.S. 156, 159, 53 S. Ct. 330, 331, 77 L. Ed. 670, that: 'The Government concedes that if assets of the taxpayer used in trade or business or "in any transaction entered into for profit," are stolen in any year, the taxpayer sustains the loss in that year and the deduction must then be taken even though the theft is not discovered or the amount ascertained until the following year.' More direct authority for the Commissioner's view, however, is found in First National Bank of Sharon, Pa., v. Heiner, 3 Cir., 66 F. 2d 925, and Borden v. Commissioner, 2 Cir., 101 F. 2d 44.
>
> "In the First National Bank of Sharon case the United States Circuit Court of Appeals for the Third Circuit held that a loss sustained by the taxpayer through embezzlement prior to 1928, but not discovered until that year, could not be deducted as a 1928 loss, and the United States Circuit Court of Appeals for the Second Circuit ruled similarly in the Borden case, although in that case the loss was

discovered before the date for filing the return for the year when the theft occurred.

"On the other hand the Circuit Court of Appeals for the Sixth Circuit in Glenn v. Louisville Trust Co., 124 F. 2d 418, 420, held that a loss sustained by a taxpayer through the unauthorized and improvident investment of his money by an agent or trustee could be taken in 1933, the year when the loss was adjusted and settled, even though the defalcation resulted in loss in 1930 and was discovered in 1931. In this case the court concluded its opinion with the statement: 'Viewing the problem realistically, as we are enjoined to do by authorities so numerous that citation becomes superfluous, we conclude that upon whatever theory Pirtle or his estate suffered a loss through the unauthorized investment of his funds, the loss was suffered in 1933 when the extent of it first was ascertained.'

"While this case is not squarely in point, it seems to us to indicate the proper point of view from which to look at the problem presented by this phase of the case at bar. From the statute it is evident that Congress intended to permit taxpayers to deduct the net amount of their legitimate losses, but, for obvious reasons, Congress did not intend to permit a taxpayer to take a deduction for a loss in any year which might serve his interest. So, to accomplish its purpose, Congress naturally provided that losses should be taken in the year in which sustained. But, looking at the scheme devised for the taxation of incomes as a whole, and construing and applying the statute 'with a view of avoiding, so far as possible, unjust and oppressive conse-

quences', (Farmers' Loan & Trust Co. v. Minnesota, 280 U.S. 204, 212, 50 S. Ct. 98, 100, 74 L. Ed. 371, 65 A.L.R. 1000) we believe that Congress did not intend that its rule should be inelastically and rigidly applied, and this we think the Treasury Department recognized when it used the word 'ordinarily' in the last sentence of Article 43—2 of its Regulations 86.

"Doubtless in the majority of cases of the sort under consideration the end contemplated could be accomplished by filing in the year of discovery an amended return for the year of loss. But when as here no such amended returns could be filed by the petition because it was unable to determine the actual dates of the different acts of embezzlement, the results of which together caused its gross loss of nearly one hundred thousand dollars, we believe that the situation is so extraordinary that its total net loss may be deducted in the year when the loss was discovered and its extent determined, that is, 1935."

The decision in the above case has been followed as follows:

In the case of *Maria G. Miglietto* TC Memo Opinion Docket 108679 January 28, 1943, the taxpayer's funds were embezzled by her father while acting as her guardian during the years 1934 to 1938, inclusive. The taxpayer did not discover the loss until 1939 when her father told her of his misconduct. In that case The Tax Court permitted the deduction to be taken in the year 1938 where the Commissioner was attempting to impose a deficiency assessment for 1938.

In *Gwinn Bros. & Co. v. Comissioner of Internal Revenue,* 7 TC 320 (1946) the taxpayer in 1935 discovered that an employee had embezzled large sums from it commencing prior to 1932. The Commissioner allowed some deductions for the misappropriated funds for the years 1932 to 1935, leaving a balance above $44,000.00 undeducted in the latter year. The Court held that the petitioner could deduct its total net loss in 1935, which was the year the loss was discovered and its extent determined.

In *Samuel M. Felton,* 5 T.C. 256 (1945), the taxpayer in 1938 gave $20,000 to an agent to invest for him. The agent had been in the business of managing funds for others for five years under contracts permitting the intermingling of funds. In 1940 the agent absconded, and thereafter in the same year the taxpayer learned that the agent had actually been insolvent since 1933. The taxpayer claimed that the loss was deductible in 1940 when he first discovered the embezzlement, but the Commissioner contended that the loss was incurred sometime prior to 1940. The Tax Court allowed the loss in 1940, pointing out that until the agent absconded his scheme of manipulation was working, that because of the intermingling of funds it was impossible for the taxpayer to ascertain the exact year in which his own funds had been misappropriated, and that under these facts he should not be compelled to do so. The Commissioner published his acquiescence in the decision: 1945 *Cum. Bull.* 3.

Conclusion.

We believe and contend that the Treasury Department of the United States, through its Commissioner of Internal Revenue, has attempted to follow too literally and stringently the regulation that a loss from theft or embezzlement occurring in one year and discovered in another year is ordinarily deductible for the year in which sustained. *Income Tax Regulations* 111, Section 29.43—2. The word *"ordinarily"* has been lost sight of in this case. It is clear from the consideration of all of the facts in this case that the situation is here singularly *extraordinary*. The reasoning of the Court in the *Boston Consolidated Gas Company Case, supra,* is so clear that we are at a loss to understand how the Treasury Department could refuse the appellant the deduction in the manner claimed. The action of the Treasury Department in disallowing the deduction is quite unjust and oppressive to this appellant under the peculiar circumstances herein set forth. We do not believe that Congress intended that a taxpayer should be deprived unjustly of a tax deduction where the circumstances so clearly indicate that the year 1941 was the only year for which the deduction could properly be claimed. As stated by the Court in the *Boston Consolidated Gas Company Case*, it is evident from the Statute that Congress intended to permit taxpayers to deduct the net amount of their legitimate losses, but, for obvious reasons, Congress, did not intend to permit a taxpayer to take a deduction for a loss in any year which might serve his purpose. Congress did not intend, however, that its rule should be inelastically and rigidly applied.

The Court below agreed with the above conclusion, but felt bound by precedent to hold otherwise. We think the Court has unnecessarily restricted itself. If the decision in the precedent is erroneous, it may and should be overruled. Furthermore, it is our contention the precedent upon which the Court below impinged itself is clearly not in point. It therefore follows that the rule set forth by the First Circuit in the *Boston Consolidated Gas Company Case,* being the only appellate case in point, should be followed by this Honorable Court in deciding in favor of appellant herein.

In the case of *Stevenson-Chislett, Inc. v. The United States,* which is reported in 98 Fed. Supp., 252, and which case is now pending in this Court, Judge Clary, in the District Court for the Western District of Pennsylvania, held that the taxpayer was entitled to deduct the embezzlement losses in the year of discovery where the embezzlements took place in previous years but were not known to the taxpayer. We submit to the Court that the decision is correct, but contend most earnestly that there can be no distinction between that case and the instant case merely because of the fact that the taxpayer there was unable to discover the exact year of losses because the embezzler did not keep any records, where here the embezzler kept a record of what he had appropriated but which fact was entirely unknown to the taxpayer. In both cases, the deduction should be allowed in the year of discovery.

In the recent case of *Rutkin, Petitioner, v. United States of America,* decided March 24, 1952, and reported in Law. Ed. Advance Reports for April 7, 1952, Vol. 96, page 485, this Court has approved the principles involved

in *Commissioner v. Wilcox, supra*; which held that embezzled funds were not taxable income to the embezzler on the theory that the embezzler had no *bona fide* legal or equitable claim to the money, was under a definite legal obligation to return it to its rightful owner and consequently had no more received the kind of "gain" or "income" which Congress has taxed than if he had merely borrowed money. To be consistent and to follow that decision to its logical conclusion, it is clear that no loss by embezzlement could be held to be sustained until, upon discovery thereof, and the happening of contemporaneous events, such as here, the death of the insolvent embezzler, has made recovery of the "loan" impossible.

In view of the facts in this case and the law applicable thereto, as set forth above, it is respectfully urged that the Court conclude as a matter of law that appellant, Martha L. Alison, sustained a deductible loss of $21,804.90 during the year 1941, and that by reason thereof the judgment of the Court below be reversed and set aside and judgment here entered in her favor and against the defendant below in the amount of $2,843.78, with interest at six per cent (6%) on $2,711.78 from March 11, 1942, and on $132.00 from November 19, 1942.

Respectfully submitted,

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